

**MARKET CONDUCT EXAMINATION REPORT**

**of**

**THE NORTHWESTERN MUTUAL LIFE INSURANCE  
COMPANY**

**of**

**MILWAUKEE, WISCONSIN**

**As of**

**December 31, 2003**

**By**

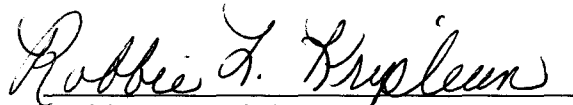
**VERMONT DEPARTMENT OF BANKING,  
INSURANCE, SECURITIES AND HEALTH CARE  
ADMINISTRATION**



## CERTIFICATION

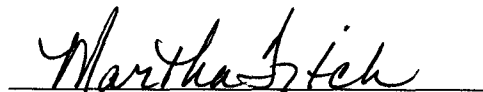
James R. Montgomery III, AIE, FLMI, MAAA, Robbie L. Kriplean, CIE, AIRC and Jennifer E. Greenway, AIRC participated in this examination.

I, Robbie L. Kriplean, CIE, AIRC, being duly sworn, do hereby affirm that the foregoing report of the Market Conduct Examination of the Northwestern Mutual Life Insurance Company is true and correct to the best of my knowledge and belief.

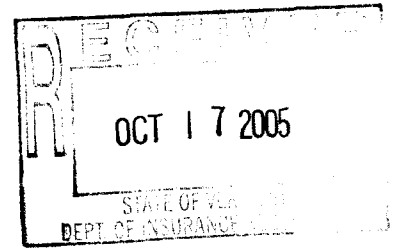
  
Robbie L. Kriplean, CIE, AIRC

Notary Seal

Subscribed and sworn to before me this 4<sup>th</sup> day of October 2005.

  
NOTARY PUBLIC

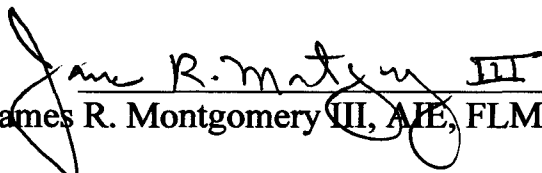
My commission expires 5/5/09



## CERTIFICATION

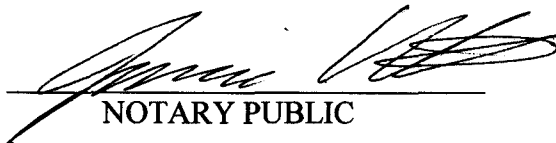
James R. Montgomery III, AIE, FLMI, MAAA, Robbie L. Kriplean, CIE, AIRC and Jennifer E. Greenway, AIRC participated in this examination.

I, James R. Montgomery III, AIE, FLMI, MAAA, being duly sworn, do hereby affirm that the foregoing report of the Market Conduct Examination of the Northwestern Mutual Life Insurance Company is true and correct to the best of my knowledge and belief.

  
James R. Montgomery III, AIE, FLMI, MAAA

Notary Seal

Subscribed and sworn to before me this 13 day of October, 2005.

  
NOTARY PUBLIC

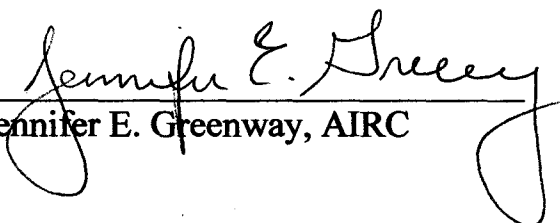


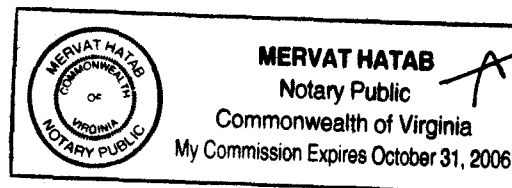
**Jamie White**  
Commission # DD475111  
Expires September 22, 2009  
Bonded Troy Fair - Insurance, Inc. 800-385-7019

## CERTIFICATION

James R. Montgomery III, AIE, FLMI, MAAA, Robbie L. Kriplean, CIE, AIRC and Jennifer E. Greenway, AIRC participated in this examination.

I, Jennifer E. Greenway, being duly sworn, do hereby affirm that the foregoing report of the Market Conduct Examination of the Northwestern Mutual Life Insurance Company is true and correct to the best of my knowledge and belief.

  
Jennifer E. Greenway, AIRC



Notary Seal

Subscribed and sworn to before me this 12<sup>th</sup> day of October, 2005.

  
NOTARY PUBLIC

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October 6, 2005

The Honorable John Crowley  
Commissioner  
Vermont Department of Banking, Insurance,  
Securities and Health Care Administration  
89 Main Street, Drawer 20  
Montpelier, Vermont 05620

Dear Commissioner Crowley:

Pursuant to your instructions and in compliance with the provisions of 8 V.S.A. § 3565 et seq. and procedures promulgated by the National Association of Insurance Commissioners, an examination of the market conduct activities has been conducted of:

The Northwestern Mutual Life Insurance Company, NAIC # 67091

Mail Address:  
720 East Wisconsin Avenue  
Milwaukee, Wisconsin 53202-4797

Statutory Home Office:  
720 East Wisconsin Avenue  
Milwaukee, Wisconsin 53202-4797

The report thereon, as of December 31, 2003, is respectfully submitted.

## **FOREWORD**

This target market conduct examination report is written generally by exception and additional practices, procedures and files subject to review during the examination were omitted from the report if no improprieties were observed.

The Northwestern Mutual Life Insurance Company is referred to throughout this report as the "Company", unless specifically mentioned by name. The Vermont Department of Banking, Insurance, Securities and Health Care Administration is referred to as the "Department" or the "Vermont Department".

The Company's responses, with respect to the findings of this examination, will be made available upon written request to the Vermont Department.

The examiners wish to acknowledge the exceptional cooperation of the Company's Audit Consultant, Joy Towell, CPA, CIA, in facilitating the examination process.

## **SCOPE OF EXAMINATION**

### **EXAMINATION AUTHORITY**

The examination of The Northwestern Mutual Life Insurance Company was conducted pursuant to applicable Vermont statutes and regulations.

### **TIME FRAME**

The examination generally covers the period from January 1, 2001 through December 31, 2003.

### **SAMPLING METHODOLOGY**

The examiners used random sampling techniques, utilizing ACL software.

### **EXAMINATION SITUS**

The Company's statutory home office is located at, 720 East Wisconsin Avenue, Milwaukee, Wisconsin 53202-4797, however, this examination was conducted entirely off-site. Information, documents and other materials were provided directly to the examiners in hard copy and/or computer diskettes.

### **MATTERS EXAMINED**

- Claims administration
- Replacements

## **PREVIOUS EXAMINATIONS**

### **PRIOR REPORT SUMMARY AND CONCLUSIONS**

The Vermont Department did not conduct an examination of the Company during the last five years.

## **EXECUTIVE SUMMARY**

### **Claims Procedures and Processing**

The Company's practice regarding death claims arising from policies issued prior to 1974, was to apply interest rates on proceeds pursuant to the laws of the insured's state of residence at the time of death, in contravention of 8 V.S.A. § 3665, for those policies issued in Vermont. The laws of the state where the policy was written are those which actually govern.

The Company's practice for death claims pertaining to policies issued during 1974 and after is to apply a programmed comparison of three (3) interest rates to include those required by the state of the insured's residence, the state of residence of the beneficiary and the state of issuance of the policy. The Company pays the highest of the three (3).

The examiners recommended that the Company's procedures be amended by requiring a copy of the original application in all cases issued prior to 1974, in order to verify the state of issue and afford the beneficiaries the same treatment as those where the policies were issued during and after 1974. The Company responded that they have amended their procedures in accordance with the examiners' recommendation.

The examiners reviewed a random sample of forty-nine (49) claim files in order to identify any violations of 8 V.S.A. § 3665 (c ) (2). This review revealed four (4) policies where the Company failed to pay the full required 6% interest on death claim proceeds. In two (2) of the cases the Company took corrective action by paying supplemental additional interest in order to bring it to 6% from the date of death until the date of the supplemental interest payment. In the other two (2) cases the supplemental interest payment did not include 6% from the date the claims were initially paid until the date the corrective action was taken.

The examiners have recommended that the Company go back as far as the Vermont Department deems appropriate and perform an audit on those claims which are subject to Vermont statutes and recalculate and pay the additional interest due using the statutory rate including interest on the additional amounts due, from the date of the initial claim payment to the date the corrective action is taken.

### **Replacements**

The examiners reviewed random samples of fifty (50) replacement files, fifty (50) issued life files and fifty (50) issued annuity files from populations of two hundred and eleven (211), nine hundred and one (901) and one hundred and fifty-two (152) respectively. The reviews revealed only three (3) violations of replacement regulations as described in the body of this report.

Regulation 2001-3 § 4 B requires companies to have the capacity to monitor each of their producers' life insurance policy and annuity contract replacements and to produce and make such records available to the Vermont Department upon request.

The examiners requested and received detailed data produced pursuant to the Regulation. After an extensive review of the data, the examiners included a number of recommendations in this report, which are offered with the thought that they may enhance the Company's system for monitoring producer replacement activity.

The Company did not require a statement from their producers, identifying any preprinted or electronically presented company approved sales materials used in connection with replacement transactions, pursuant to Regulation 2001-3 § 3 (E). The examiners recommended that the Company require its producers to complete a statement identifying sales materials used in replacement transactions.

## **COMPANY PROFILE**

### **HISTORY**

The Company was incorporated on March 1, 1857, as Mutual Life Insurance Company of Wisconsin and commenced business on November 25, 1858. The present title was adopted in 1865.

The core business is individual life insurance, which represents over 80% of the Company's total premium production. Products include traditional and variable life insurance in addition to disability insurance and fixed and variable annuities.

The agencies are operated as independent business units, each of which is responsible for "its own" operating profitability. This has resulted in high agent retention rates and very favorable persistency experience. Lapse rates for individual life insurance have been ranging from 4 to 4.5%.

The Company is licensed in all states and the District of Columbia. Their 2002 market share of total life companies in Vermont was 3.5%, which made them the sixth largest writer in the state.

### **STATUTORY HOME OFFICE**

720 East Wisconsin Avenue  
Milwaukee, Wisconsin 53202-4797

## VERMONT REPORTED PREMIUMS

Direct written premiums in Vermont for the years indicated are as follows:

	<b>2001</b>	<b>2002</b>	<b>2003</b>
<b>Individual Life</b>	7,719,132	7,849,095	8,396,506
<b>Individual Annuities</b>	2,476,718	2,323,871	1,821,864
<b>Accident &amp; Health</b>	1,049,910	1,045,542	1,077,538
<b>Deposit</b>	0	190,000	149,867
<b>Other</b>	26,145	13,378	23,474
<b>Totals</b>	11,271,905	11,421,886	11,469,249

## **(I) CLAIMS PROCEDURES AND PROCESSING**

### **(A) SAMPLE SELECTION**

The examiners requested fifty (50) claim files which were randomly selected with the use of ACL software. The listing the Company provided, from which the sample was drawn, contained one hundred and eighty-one (181) records representing life claims paid during the examination period. Of the fifty (50) initially requested files, eighteen (18) were disallowed from the review as five (5) cases were life policies not issued in the state of Vermont and therefore not subject to the examination, two (2) were annuity claims and the remaining eleven (11) were duplicates. An additional sample of eighteen (18) was requested in order to achieve a total sample size of fifty (50) cases in accordance with NAIC guidelines. Of the eighteen (18) additional files provided, the examiners disallowed five (5) as they were life policies not issued in Vermont. A third request for an additional ten (10) files produced four (4) files which, were subject to the review.

In summary, a total of seventy-eight (78) files were requested. Out of that total, forty-nine (49) claim files were determined to be appropriate samples and subject to the examination.

The difficulty the examiners encountered in securing an appropriate number of files was primarily due to the fact that the Company's computer systems precluded the capturing of issue state data for policies issued prior to 1974.

### **(B) INTEREST PAYMENT PROCEDURES**

Regarding the application of interest rates to life claim proceeds, the Company's practice was to apply the interest rate appropriate to the state of residence of the insured (at the time of death) for those cases issued prior to 1974, which contravenes 8 V.S.A. § 3665 (For those policies issued in the state of Vermont).

Notwithstanding the above described procedure, the Company's standard practice for those policies issued on or after 1974, was to apply a programmed comparison of three (3) interest rates which include rates required by the state of residence of the insured, the state of residence of the beneficiary and the state of issuance of the policy. The highest rate of interest among the rates was then paid to the beneficiary. The examiners criticized the Company for not affording the same benefit (the highest programmed rate of interest) to those beneficiaries of the life policies issued prior to 1974.

Further, the examiners recommended that the Company amend their procedures by requiring a copy of the original application in all cases issued prior to 1974 in order to verify the state of issue and afford the beneficiaries the same treatment as those cases issued on or after 1974.

The Company responded on August 10, 2004, that they amended their procedures as follows:

*Upon receipt of notice of death of an insured, all contracts pertaining to the insured will be reviewed. If any of the contracts were issued prior to 1974, the applications will be requested prior to case assignment. The applications will then be reviewed to determine the state of issue.*

### **(C) VIOLATIONS OF 8 V.S.A. § 3665 (c) (2)**

The findings of the review of the forty-nine (49) sample claim files are described below:

<b>Policy #</b>	<b>Comments</b>
6359098	Violation of 8 V.S.A. § 3665 (c) (2) Did not pay 6 % interest
7867353	Violation of 8 V.S.A. § 3665 (c) (2) Did not pay 6 % interest
8425587	Violation of 8 V.S.A. § 3665 (c) (2) Did not pay 6 % interest
8391040 (Same insured as above)	Violation of 8 V.S.A. § 3665 (c) (2) Did not pay 6 % interest

The examiners criticized the Company for the violations identified in the above chart. Subsequently the Company initialed corrective action as discussed below.

- **Policy # 6359098**

This claim was paid 4-28-03, which was within what the Company refers to as the “system malfunction” period (refer to the discussion under “**D-System Malfunction**”). Even though the Company’s report, (generated to identify the interest rate errors that may have occurred during this period) detected this claim, the Company failed to pay the required interest rate. The Company’s response was: “unfortunately, this claim was overlooked during the review process.”

The Company undertook corrective action by sending a letter and draft dated 8-23-04, to the beneficiary stating that additional interest should have been paid when the claim was settled and that they were attaching a draft “which represents an additional 2.5% in interest on the proceeds”.

- **Policy # 7867353**

The Company’s corrective action with respect to the claim referenced above, as in the case regarding policy # 6359098, was to send a letter and draft dated 8-23-04, to the beneficiary paying an additional 2.5% in interest on the proceeds.

- **Policy # 8425587 and 8391040**

Regarding the above referenced cases, the Company's corrective action involved issuing a draft in the amount of \$1,193.27 to the beneficiary reflecting an additional 2.5% interest from April 21, 2003 (date of death) through June 4, 2003 (date claim was initially paid), and 6% interest from June 4, 2003 through June 30, 2004 (Date the additional interest was paid).

### **(1) Recommendation**

The examiners note, with regard to policies # 6359098 and # 7867353, that the Company's corrective action was to pay an additional **2.5%** in interest on the proceeds. Conversely, with respect to policies # 8425587 and #8391040, in addition to paying the additional 2.5% interest on the proceeds, the Company paid **6%** interest from the date of the initial payment through the date the corrective action was taken (6-30-04).

The examiners recommend that, in the cases identified as policies # 6359098 and # 7867353, the Company pay 6% interest from the date the claim was initially settled through the date corrective action was taken (8-23-04) as in the cases identified as policies numbered 8425587 and 8391040.

### **(D) SYSTEM MALFUNCTION**

#### **Policies Numbered: 5801883, 4332772, 6115168 & 6994267 (Same Insured)**

The review of the above referenced claim file revealed that an incorrect rate of interest (3.5%), not the statutorily required rate of 6%, was applied due to a "system error". The Company stated that "the error was detected when the Life Benefits Information Systems contact noticed that the rate table that normally applies to those cases was not present in the payment system." The claim was initially paid May 2, 2003. Apparently the "error" was not detected until the additional interest due the beneficiary was paid on December 22, 2003.

The examiners inquired as to how widespread the problem was, to what extent Vermont insureds were affected and what steps the Company took in order to correct the "malfunction". The Company responded that "the interest rate problem resulting from a system malfunction affected policies paid from April 7, 2003 through May 7, 2003. The problem affected policy benefits paid to beneficiaries in states where a rate higher than Northwestern Mutual's contract rate applied. This affected a total of 159 payments for all states over the one-month span. A report was generated and all of the affected cases were reviewed and a manual payment was made to correct the interest amount." (Emphasis added)

Further, the Company added: "Since this occurrence, Information Systems has received documentation to insure that this table is not deleted when repairs or upgrades are done. It was during one of these upgrades that the table was deleted."

Refer to the discussion under (C ) **VIOLATIONS OF 8 V.S.A. § 3665 (c ) (2).**

**(E) VIOLATION OF 8 V.S.A. § 3665 (d)**

The Company's practice with respect to payments of claims under policies of life insurance, which is to pay interest at the rate of 6% in the event a claim is not paid within 30 days of receipt of due proof of loss, contravenes 8 V.S.A. § 3665 (d). The statute provides that if an insurer fails to pay a claim timely (within 30 days of receipt of proof of loss), interest shall accrue from thirty days after the receipt of proof of loss and shall be the judgment rate allowed by law, which in Vermont is 12%.

The Company's response to the examiners' criticism was that "Northwestern Mutual agrees that, pursuant to Section 3665, the penalty rate of 12% should be applied for policies of life insurance under those circumstances set forth in Section 3665. The company is in the process of updating its claim payment system to reflect that rate."

**(F) RECOMMENDATION**

It is recommended that the Company go back as far as the Vermont Department deems appropriate and perform an audit on those claims which are subject to Vermont statutes and recalculate and pay the additional interest due using the statutory rate including interest on the additional amounts due, from the date of the initial claim payment to the date the corrective action is taken.

## **(II) REPLACEMENTS**

The examination period for this report runs from January 1, 2001 to December 31, 2003. Vermont Regulation 2001-3 became effective on March 1, 2002, and replaced Regulation 88-2, which was in effect prior to that time. Tests were performed in order to determine compliance with these regulations as described below.

### **(A) REPLACEMENT REVIEW**

The examiners selected a random sample of fifty (50) files from a population of two hundred and eleven (211) files listed in the Company's replacement register, for review in order to determine compliance with applicable replacement regulations.

Out of the sample of fifty (50) replacement files reviewed, the examiners identified one (1) violation of Vermont Regulation 88-2. File # 15783458 did not contain a Notice Regarding Replacement as required by Regulation 88-2 § 8 (C) due to an apparent misfiling.

### **(B) ISSUED LIFE AND ANNUITY REVIEW**

The tests performed by the examiners involved reviewing a random sample of fifty (50) issued life policy files, out of a population of nine hundred and one (901) and a random sample of fifty (50) annuity files, out of a population of one hundred and fifty-two (152). The samples represented those policies/contracts that were issued within the examination period and were reviewed for compliance with Vermont Regulation 2001-3, effective on March 1, 2002, or Regulation 88-2, which was in effect prior to that time.

#### **(1) Issued Life Sample**

Two (2) violations of Vermont Regulation 88-2 were observed in the issued life sample review. Both violations were noted in life policy # 16013624. The Company failed to furnish the required Notice Regarding Replacement, in violation of Regulation 88-2 § 8 (C). Additionally, the Company failed to provide evidence that written communication was sent to the existing insurer within five (5) business days pursuant to Regulation 88-2 § 8 B (2). The Company stated that their internal processes did not detect that this policy was a replacement.

In completing the application for this policy (# 16013624), the applicant answered the replacement question "no", indicating that the policy was not a replacement. Conversely, the applicant indicated "yes" as to whether insurance with other companies would be replaced. The agent answered the replacement question "yes" (in the agent's section of the application), indicating that the policy was a replacement. The application was never determined to be a replacement by the Company's computer system since the applicant's replacement question was answered "no". A "replacement discrepancy edit" was generated by the underwriter's computer system, which according to the Company "was apparently missed, as the case was approved without the Replacement Compliance Division ever becoming aware of the discrepancy."

The examiners recommend that the Company modify their processes to better detect replacements. The Company should require that answers to all of the questions on the application regarding replacement be input into the computer system to ensure that an error in one question would not prevent the Replacement Compliance Division from becoming aware of the replacement. In addition, this would also ensure that if the input processor made a data entry error in entering one of the replacement questions from the application into the computer system, the application would automatically be downloaded to the Replacement Compliance Division. This would eliminate the need for the underwriter to notify the replacement division upon the computer generating a replacement discrepancy edit report, which, in this case, never occurred. Regulation 2001-3 § 4 requires insurers to comply with the regulation by instituting procedures to detect replacements that have not been reported as such by the applicant or producer. The Company stated that, "as a result of this review, we are currently evaluating solutions to prevent these types of replacement discrepancies from being missed".

### **(2) Issued Annuity Sample**

One violation of Regulation 2001-3 § 4 (C) was observed in the issued annuities sample. Contract # 16044112 did not contain a statement signed by both the applicant and the producer as to whether the applicant had existing policies or contracts pursuant to the Regulation.

The Company responded that the application for this contract was completed twelve (12) days after the effective date of Regulation 2001-3. The Company's current application, does include the statement required by Regulation 2001-3 § 4 (C).

### **(3) Summary of Issued Life and Annuity Review**

In summary, the review of the fifty (50) issued life insurance policy files and fifty (50) issued annuity contract files revealed two (2) policies containing three (3) violations. The

examiners observed that the Company made a diligent effort to comply with the requirements of Regulation 88-2 and Regulation 2001-3 as violations were found in only two percent (2%) of the files reviewed.

### **(C) MONITORING PROCEDURES**

Vermont Regulation 2001-3 § 4 B requires that companies have the capacity to monitor each producer's life insurance policy and annuity contract replacements and to produce and make such records available to the Vermont Department upon request. The capacity to monitor shall include the ability to produce records for each producer's:

- (1) Life replacements, including financed purchases, as a percentage of the producer's total annual sales for life insurance;*
- (2) Number of lapses of policies by the producer as a percentage of the producer's total annual sales for life insurance;*
- (3) Annuity contract replacements as a percentage of the producer's total annual annuity contract sales;*
- (4) Number of transactions that are unreported replacements of existing policies or contracts by the existing insurer detected by the company's monitoring system as required by Subsection A (5) of this section; and*
- (5) Replacements, indexed by replacing producer and existing insurer.*

The examiners requested all of the above information regarding two (2) selected producers, in order to verify compliance with § 4 B of the Regulation.

From the data furnished to the examiners, in response to this request, it was noted that there were thirty-two (32) internal replacements listed for one of the producers and twenty (20) listed for the other. When the examiners made further inquiry about these internal replacements, the Company responded that eighteen (18) of the thirty-two (32) internal replacements attributed to one of the producers and eleven (11) of the twenty (20) attributed to the other, were "Term Conversions or Term Upgrades". These "Term Conversions" were represented by the Company as being conversions resulting from the exercise of contractual conversion privileges. This being the case, the examiners recommend that such policies not be included with information required by Regulation 2001-3 § 4 B inasmuch as contractual conversions are specifically exempted from the Regulation pursuant to § 1 B (4). The inclusion of policies that are not within the scope of the Regulation merely skews the data, thereby making it more difficult to monitor a producer's replacement activity regarding those replacements which are required to be monitored.

The examiners further observed that the number of life replacements reported in the data that the Company provided for the two (2) selected producers, pursuant to Regulation 2001-3 § 4 B (5), did not match the number of life replacements shown in their report of total life replacements as a percentage of total sales reported pursuant to § 4 B (1) of the Regulation.

The Company explained that the data for life replacements, including financed purchases, as a percentage of the producer's annual sales (Regulation 2001-3 § 4 B (1)) is obtained from their Underwriting Standards Department and includes only those policies that were issued by the New Business section and actually put in force (and therefore count as "sales."). The "sales" data does not include policies that were declined by the New Business section, or not taken by the client. The spreadsheets furnished pursuant to Regulation 2001-3 § 4 B (5), however, came from the Replacement Compliance System and contain a different set of data, maintained for a different purpose. Thus, one set of data includes "declined" and "not taken" policies as replacements and the other does not.

The examiners recommend that the Company use consistent data in the preparation of the various reports listed in Regulation 2001-3 § 4 B (1) through (5).

The Company uses Sales Monitoring Reports (SMR) to monitor their producers' internal replacements, external replacements, sales that may have used inforce values, 13<sup>th</sup> month lapses and policy changes. The SMR reports are exception reports, produced every six months that list producers whose averages exceed those averages of their peer group (Northwestern Mutual producers with similar years of experience) multiplied by an "Adjustment Spread" factor. The Adjustment Spread factor varies with the number of sales. The Company produced charts with various categories of numbers of sales and the corresponding Adjustment Spread factor. The Adjustment Spread factors decrease as the number of sales increase. For example, an agent with 12 sales would have a higher Adjustment Spread factor than an agent with 22 sales. There are separate charts for Adjustment Spread factors for internal replacements, external replacements, sales that may have used inforce values, 13<sup>th</sup> month lapses and policy changes.

The examiners contend that the spreads derived by the Company's method, are too broad to properly monitor an agent's replacement activity. For example, if an agent sold 40 policies, he would only be flagged by the SMR if his internal replacement average exceeded **5.8 times** the average of his peers. The examiners assert that 5.8 times the average of the producers' peers is too broad of a criterion to use because it is so much higher than the peers' average. In addition, this is only an initial exception used to monitor producers' activity. The Company explained that "only those agents who meet at least one of the following second level selection criteria will appear as a "final exception" on the final SMR for that specific period:

- Agent qualifies for an “initial exception” in more than one SMR exception category (internal replacement, external replacement, sales that may have used inforce values, 13<sup>th</sup> month lapses, policy changes) in the same 6-month SMR period. –OR–
- Agent qualifies for an “initial exception” in the internal replacement category on the current SMR, and the agent qualified for at least one initial exception for internal replacements on the previous SMR run –OR–
- Agent’s internal replacement average is 1.5 times greater than the peer group adjusted average for internal replacements.”

The examiners contend that the initial exception criteria are too broad and because the requirements of the second level selection criteria must also be met for an agent’s replacement activity to be flagged by the SMR, the likelihood is significant that excessive replacement activity by an agent could go undetected by the Company.

The examiners recommend that the Adjustment Spreads used for flagging agents’ replacement activity be more restrictive and that the second level selection criteria be eliminated. If an agent has replacement or lapse rate averages that are not in line with those of his peers, this should be sufficient criterion to warrant further investigation.

#### **(D) PRODUCER’S STATEMENT IDENTIFYING SALES MATERIALS**

Vermont Regulation 2001-3 § 3 (E) requires that, “except as provided in Section 5C, in connection with a replacement transaction the producer shall submit to the insurer to which an application for a policy or contract is presented, a copy of each document required by this section, a statement identifying any preprinted or electronically presented company approved sales materials used, and copies of any individualized sales materials, including any illustrations related to the specific policy or contract purchased”.

The Company stated that they do not make use of the alternative provided for in Regulation 2001-3 § 5 (C) and that they comply with Regulation 2001-3 § 3 (E). The Company failed to obtain statements from the producers identifying any preprinted or electronically presented company approved sales materials used. In fact, the Company did not require such a statement from its producers.

The Company indicated that they require their producers to submit with the application, actual copies of sales materials presented to the client instead of accepting a statement from the producer identifying which sales materials were used. This practice is not compliant with the regulation, which requires a statement in addition to the other specified items identified in § 3 (E).

The examiners recommend that the Company require its producers to complete a statement identifying any preprinted or electronically presented company approved sales materials used in connection with replacement transactions.

## **SUMMARY OF RECOMMENDATIONS**

**1.**

### **Page 9**

The examiners recommended that the Company's claims procedures be amended by requiring a copy of the original application in all cases where the policy was issued prior to 1974, in order to verify the state of issue and afford the beneficiaries the same treatment as those where the policies were issued during and after 1974. The Company informed the examiners that they have amended their procedures in accordance with the examiners' recommendation.

**2.**

### **Page 10 & 11**

Supplemental interest on the proceeds of two (2) claims did not include 6% from the date the claims were initially paid until the date the corrective action was taken. The examiners recommend that this be rectified.

**3.**

### **Page 12**

It is recommended that the Company go back as far as the Vermont Department deems appropriate and perform an audit on those claims which are subject to Vermont statutes and recalculate and pay the additional interest due using the statutory rate including interest on the additional amounts due, from the date of the initial claim payment to the date the corrective action is taken.

**4.**

### **Page 14**

The examiners recommended that the Company modify their process to better detect replacements. The Company indicated that, as a result of the examiners' review, they are currently evaluating solutions to prevent these types of replacement discrepancies from being missed.

5.

**Page 15**

It is recommended that life insurance replacement policies resulting from contractual conversions not be included with information required by Regulation 2001-3 § 4 B., inasmuch as such policies are not within the scope of the Regulation and merely skew the data, thereby making it more difficult to monitor a producer's replacement activity regarding those replacements which are required to be monitored.

6.

**Page 15 & 16**

The examiners recommend that the Company use consistent data in the preparation of the various reports listed in Regulation 2001-3 § 4 B (1) through (5).

7.

**Page 17**

The examiners recommend that the Adjustment Spreads used for flagging agents' replacement activity be more restrictive and that the second level criteria be eliminated.

8.

**Page 17 & 18**

The examiners recommend that the Company require its producers to complete a statement identifying any preprinted or electronically presented company approved sales materials used in connection with replacement transactions, in compliance with Vermont Regulation 2001-3 § 3 E.